United States Court of Appeals

for the Second Circuit

SUPPLEMENTAL BRIEF

75-7404

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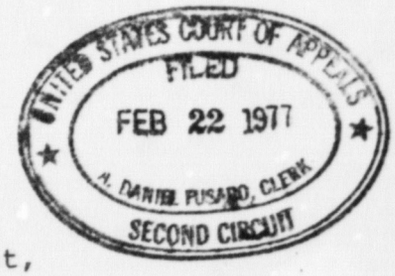
FOR THE SECOND CIRCUIT



No. 75-7404

ARNOLD MARSHEL,

Plaintiff-Appellant,

v.

AFW FABRIC CORP., CONCORD FABRICS, INC.
ALVIN WEINSTEIN and FRANK WEINSTEIN,

Defendants-Appellees.

BARRY L. SWIFT,

Plaintiff-Appellant,

v.

CONCORD FABRICS, INC., AFW FABRIC CORP.,
ALVIN WEINSTEIN and FRANK WEINSTEIN,

Defendants-Appellees.

MEMORANDUM OF PLAINTIFFS-APPELLANTS ARNOLD MARSHEL and BARRY L. SWIFT ON THE POINT OF MOOTNESS

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MEMORANDUM OF PLAINTIFFS-APPELLANTS ARNOLD MARSHEL AND BARRY L. SWIFT ON THE POINT OF MOOTNESS

In accordance with this Court's order of January 21, 1977, plaintiffs-appellants, Arnold Marshel, and Barry L. Swift, ("plaintiffs") respectfully submit this memorandum in support of their position that the instant case is not moot.

Prior Proceedings

By opinion and order dated February 13, 1976, reported at 533 F.2d 1277, this Court reversed an order of the United States District Court for the Southern District of New York denying plaintiffs' motions for a preliminary injunction against a proposed merger between defendants, Concord Fabrics, Inc. ("Concord") and AFW Fabric Corp. ("AFW"). In reversing, this Court held that the proposed merger,

> "amounts to...a scheme by the appellees, having previously taken advantage of public financing, to appropriate for their personal benefit the entire stock ownership of Concord at a price determined by them and paid out of the corporate treasury at a cost of over $1,600,000. Such conduct is proscribed by the language of Section 10(b) and Rule 10b-5." (533 F.2d at 1280-81).

On March 10, 1976, in a per curiam opinion reported at 533 F.2d 1309, this Court denied a rehearing en banc in both the instant case and in the unrelated case of Green v. Santa Fe Industries, Inc., 533 F.2d 1283 (2d Cir. 1976), stating that it did so "not because we believe these cases are insignificant, but because they are of such extraordinary importance that we are confident the Supreme Court

will accept these matters under its certiorari jurisdiction...." (533 F.2d at 1310).

On or about June 7, 1976, the defendants filed a petition with the Supreme Court for a writ of certiorari to this Court. In their petition, only the following two questions were presented:

> "1. Did the Court of Appeals improperly expand Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 thereunder, by enjoining a merger as a 'fraud' despite the fact that all the terms, purposes and consequences of the merger and all the material facts relating thereto were fully disclosed to shareholders and there was no misrepresentation, omission or deception?
>
> "2. Did the Court of Appeals improperly expand Section 10(b) and Rule 10b-5 into an area traditionally governed by state corporate law by enjoining a merger as a 'fraud' despite the absence of any deception and despite the validity of the merger under the law of the state of incorporation?" (p. 4 of Petition For A Writ of Certiorari).

Both of the questions which defendants had presented in their petition to the Supreme Court related to the propriety of this Court's invocation of Section 10(b) of the Securities Exchange Act of 1934 in order to reverse the denial of a preliminary injunction against a merger.

However, the merger could in no event any longer take place because of the issuance of a permanent injunction by the New York State Supreme Court following this Court's Order of February 13, 1976. On March 9, 1976 defendants had consented to the entry in the state court of a permanent injunction in an action which had been commenced by the Attorney General of the State of New York under the Martin Act, N. Y. General Bus. Law §352.* By its terms the defendants were:

> "... permanently enjoined, barred and restrained from directly or indirectly effectuating the proposed merger of Concord and AFW, the terms of which merger are set forth in a Notice of Special Meeting of Shareholders of Concord dated March 17, 1975 and the accompanying Proxy Statement, and from any act in aid or furtherance of the merger."

A copy of the permanent injunction is annexed as an appendix to this memorandum.

Accordingly, plaintiff suggested to the Supreme

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* The initial opinion of the New York State Supreme Court granting a preliminary injunction against the merger was referred to by this Court in its opinion at 533 F.2d 1280, n.3.

Court, citing De Funis v. Odegaard, 416 U.S. 312 (1974) and Golden v. Zwickler, 394 U.S. 103 (1969), that the questions which defendants had presented for review had been rendered moot.

On October 12, 1976, the Supreme Court entered the following order:

> "The petition for a writ of certiorari is granted. The judgment is vacated and the case is remanded to the United States Court of Appeals for the Second Circuit to consider whether or not the case is moot."

THE CASE IS NOT MOOT

Although the questions which defendants had presented to the Supreme Court for review have been rendered moot by virtue of the subsequent issuance of the permanent injunction barring the proposed merger,* the case itself still presents justiciable controversies between actively adverse parties.

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* Cf., Irvine v. California, 347 U.S. 128, 129-30 (1954): "We granted certiorari on a petition which tendered four questions....The issues here are fixed by the petition unless we limit the grant, as frequently we do to avoid settled, frivolous or state law questions."

Both the Marshel and Swift actions were brought derivatively on behalf of Concord. In addition to seeking a judgment which would have preliminarily and permanently enjoined defendants from taking any action toward or with a view to consummating a merger upon terms which would divest Concord's public shareholders of their equity interest, the complaint in the Marshel action contains a prayer for relief which seeks to have "the individual defendants and AFW Fabric Corp. account to Concord and the Class for all damages and injury sustained by Concord and the Class as a result of the fraudulent, illegal and wrongful acts and transactions complained of herein." (paragraph (c) of prayer for relief in Marshel amended complaint). A similar prayer for relief is contained in the Swift complaint.*

The damages being sought include all monies which Concord has thus far spent in connection with the efforts of AFW and the individual defendants to take Concord private. Thus, at page 18 of the merger proxy statement, Concord estimated that its expenses were

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* The amended complaint in Marshel is set forth at pages 4-23 of the Appendix which had been filed with this Court at the time plaintiffs submitted their original brief. The complaint in Swift is set forth at pages 141-156 of the Appendix.

approximately $87,000. (p. 85 of Appendix). In addition to that sum, Concord may also have been charged for legal and other expenses which properly should be borne by AFW and the individual defendants. These out-of-pocket expenses were imposed upon Concord for no corporate purpose and are consequential damages resulting from the proposed fraudulent merger.

It is now settled that a defrauded party may, in an appropriate case, recover not only "direct" damages for violations of the federal securities laws but also "consequential" damages -- those additional expenditures attributable to the defendants' conduct which would not have been incurred but for that conduct. E.g., Chris-Craft Industries, Inc. v. Piper Aircraft Corp., 516 F.2d 172, 191 (2d Cir. 1975), cert. granted, 96 S. Ct. 1505 (1976); Foster v. Financial Technology, Inc., 517 F.2d 1068 (9th Cir. 1975); Madigan, Inc. v. Goodman, 498 F.2d 233, 238-40 (7th Cir. 1974); Zeller v. Bogue Electric Manufacturing Corp., 476 F.2d 795, 803 (2d Cir.), cert. denied, 414 U.S. 908 (1973); Esplin v. Hirschi, 402 F.2d 94, 105 (10th Cir. 1968), cert. denied, 394 U.S. 928 (1969). Consequential damages may also be recovered for common law fraud. W. Prosser, The Law of Torts § 110, at 735 (4th ed. 1971).

In short, although the merger has been prevented, those aspects of the case which seek the recovery of monetary damages still remain to be litigated.

CONCLUSION

This Court should determine that the case is not moot and should remand it to the District Court for further proceedings consistent with its opinion of February 13, 1976.

Respectfully submitted,

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LIPPER, LOWEY & DANNENBERG and
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759-1504

Dated: New York, New York
February 22, 1977

APPENDIX

Final Judgment

At a Special Term, Part II, of the Supreme Court of the State of New York, held in and for the County of New York, at the Courthouse, Pearl and Centre Streets, Borough of Manhattan, State of New York, on the 9th day of March, 1976.

Present:

Hon. XAVIER C. RICCOBONO, Justice

Index No. 40678/75

PEOPLE OF THE STATE OF NEW YORK,

Plaintiff,

against

CONCORD FABRICS, INC., AFW FABRIC CORP., ALVIN WEINSTEIN, FRANK WEINSTEIN and DAVID R. CAPLAN,

Defendants.

The plaintiff brought this action pursuant to section 353 of the General Business Law of this State by the service of a summons and complaint upon the above named defendants seeking a judgment permanently enjoining and restraining said defendants from consummating a proposed merger of Concord Fabrics Inc. ("Concord") and AFW Fabric Corp. ("AFW"), the terms of which merger are set forth in a Notice of Special Meeting of Shareholders of Concord dated

March 17, 1975 and the accompanying Proxy Statement, as well as from violating the provisions of Article 23-A of the General Business Law of this State.

Now, on reading and filing the summons dated April 4, 1975; the complaint verified on April 4, 1975; the affidavit of Eugene D. Berman, Deputy Assistant Attorney General, sworn to April 4, 1975; the affidavit of Sidney J. Silberman, sworn to April 15, 1975; and the consents of the defendants in which they specifically deny each and every allegation of the complaint herein and the aforementioned affidavit of Eugene D. Berman, and due deliberation having been had,

On motion of Louis J. Lefkowitz, Attorney General of the State of New York, attorney for plaintiff, it is

ORDERED, ADJUDGED AND DECREED that the defendants be permanently enjoined, barred and restrained from directly or indirectly effectuating the proposed merger of Concord and AFW, the terms of which merger are set forth in a Notice of Special Meeting of Shareholders of Concord dated March 17, 1975 and the accompanying Proxy Statement, and from any act in aid or furtherance of the merger; and it is further

ORDERED, ADJUDGED AND DECREED that the defendants be permanently enjoined, barred and restrained from directly or indirectly engaging in any fraudulent practice as defined in section 352(1) of the General Business Law of this State, in connection with any tender offer or merger or other transaction for the purpose of returning Concord to the private ownership of the individual defendants Alvin and

Frank Weinstein or members of their families; and it is further

ORDERED, ADJUDGED AND DECREED that the Attorney General of the State of New York may take such further application under the provisions of this judgment and decree as plaintiff may be advised is proper and necessary for the enforcement of this judgment and decree, all pursuant to Article 23-A of the General Business Law of this State and other provisions of law applicable thereto; and it is further

ORDERED, ADJUDGED AND DECREED that costs be awarded to plaintiff pursuant to section 8303(a)(6) of the Civil Practice Law and Rules in the total amount of Six Thousand Five Hundred Dollars ($6,500.00), consisting of Two Thousand Dollars ($2,000.00) in respect of AFW, Two Thousand Dollars ($2,000.00) in respect of Alvin Weinstein, Two Thousand Dollars ($2,000.00) in respect of Frank Weinstein and Five Hundred Dollars ($500.00) in respect of David R. Caplan.

Enter

XCR
J. S. C.

Norman Goodman
Clerk

FILED
Mar 10 1976
New York
Co. Clerk's Office

RECEIVED

D 2-22-77 at 11:40 a.m

KAYE, S & HANDLER

Attorneys for Defts.-appellees